

701—53.3(422) Capital loss carryback.

53.3(1) Capital losses shall be allowed or allowable for Iowa corporation income tax purposes to the same extent they are allowed or allowable for federal corporation income tax purposes. Capital loss carrybacks shall be treated as an adjustment to federal taxable income to arrive at net allocable and apportionable income.

a. For accrual-basis taxpayers the federal income tax refund shall not be accrued to the loss year but rather treated as a reduction in federal income tax paid in the carryback year.

b. Cash-basis taxpayers shall include the federal income tax refund in Iowa taxable income in the year received.

c. Where the taxpayer files a separate Iowa corporation income tax return but files as part of a federal consolidated income tax return, the portion of the federal refund due to a capital loss carryback attributable to the taxpayer shall be calculated by computing the federal tax deduction in the carryback year as follows:

Separate Company Income –
Separate Company Capital
Loss Carryback

×

Consolidated
Federal Tax
after Capital
Loss Carryback

×

50%

Sum of the Incomes of Profit
Companies – Sum of Separate
Company Capital Loss
Carrybacks to Profit
Companies

53.3(2) When the carryback year has both allocable and apportionable capital gains, the capital loss carryback shall be applied pro rata on a percentage basis of the specific gain to the total gains.

EXAMPLE: Assume a taxpayer has a 1973 capital loss carryback available of \$2000. The loss would be applied in the following manner:

| 1970 <u>Total Capital Gain</u> | 1970 <u>Allocable Gain</u> | 1970 <u>Apportionable Gain</u> |
|--|-------------------------------|--|
| \$16,000 | \$4,000 | \$12,000 |
| Allocable gain | –\$4,000 | |
| Total capital gain | –\$16,000 | = ¼ or 25% of carryback to allocable gain |
| 1970 allocable capital gain after application of loss carryback: \$4,000 less (\$2,000 × 25%) = \$3,500 net allocable capital gain. | | |

This rule is intended to implement Iowa Code sections 422.35 and 422.37.

701—53.4(422) Net operating and capital loss carrybacks and carryovers. If the taxpayer has both a net operating loss and a capital loss carryback to a prior tax year, the capital loss shall be carried back first and then the new operating loss offset against any remaining income.

This rule is intended to implement Iowa Code section 422.35.

701—53.5(422) Interest and dividends from federal securities. See rule 701—40.2(422) for a discussion of the exempt status of interest and dividends from federal securities.

This rule is intended to implement Iowa Code section 422.35.

701—53.6(422) Interest and dividends from foreign securities, and securities of state and their political subdivisions. Interest and dividends from foreign securities and from securities of state and their political subdivisions are to be included in Iowa taxable income. Certain types of interest and dividends, because of specific exemption, are not includable in income for federal tax purposes. To the extent such income has been excluded for federal income tax purposes, unless the item of income is specifically exempted from state taxation by the laws or constitution of Iowa or of the United States, it must be added to Iowa taxable income. See rule 701—40.3(422) for a listing of obligations of the state of Iowa and its political subdivisions, the interest from which is exempt from Iowa corporation income tax. For the tax treatment of interest or dividends from regulated investment companies (mutual funds) that invest in obligations of the type discussed in rule 701—40.3(422), see rule 701—40.52(422).

For tax years beginning on or after January 1, 1987, add dividends received from regulated investment companies exempt from federal tax under Section 852(b)(5) of the Internal Revenue Code and subtract the loss on the sale or exchange of a share of a regulated investment company held for six months or less to the extent the loss was disallowed under Section 852(b)(4)(B) of the Internal Revenue Code.

For tax years beginning on or after January 1, 2001, add, to the extent not already included, income from the sale of obligations of the state of Iowa and its political subdivisions. Gains or losses from the sale or other disposition of bonds issued by the state of Iowa or its political subdivisions shall be included in Iowa taxable income unless the law authorizing these obligations specifically exempts the income from the sale or other disposition from Iowa corporation income tax.

This rule is intended to implement Iowa Code section 422.35 as amended by 2001 Iowa Acts, House File 715.

701—53.7(422) Safe harbor leases. For tax years ending after January 1, 1981, deductions in determining federal taxable income for sale-leaseback agreements taken as a result of the application of Section 168(f)(8) of the Internal Revenue Code shall be added in determining Iowa taxable income to the extent such deductions cannot be taken under provisions of Sections 162, 163 and 167 of the Internal Revenue Code. The lessor shall add depreciation and interest expense, and the lessee shall add rental expense. When the deduction for depreciation is not allowed under a previous provision of this rule, the lessee shall be allowed a deduction for depreciation on any property involved in a sale-leaseback agreement. This depreciation shall be computed in accordance with Section 168(a) of the Internal Revenue Code. Income received as a result of a sale-leaseback agreement shall be deducted in determining Iowa taxable income. The lessee shall deduct interest income and the lessor shall deduct rent income. Each lessor and lessee corporation shall include a copy of federal Form 6793 in its Iowa corporation income tax return for the year in which a safe harbor lease is entered into.

This rule is intended to implement Iowa Code section 422.35.

701—53.8(422) Additions to federal taxable income.

53.8(1) Disallowance of private club expenses.

a. Expenses incurred on or after July 1, 1991, through December 31, 1993, with respect to expenditures made at, or payments to, a club which restricts membership or the use of its services or facilities on the basis of age, sex, marital status, race, religion, color, ancestry, or national origin are disallowed as a deduction and, therefore, must be added to federal taxable income. For the purposes of this rule, restricting membership or use of services or facilities due to a legal age requirement is not considered to be discrimination.

b. Definitions for the purposes of this rule.

(1) The term “*expenses*” means those expenses otherwise deductible under Section 162(a) of the Internal Revenue Code and includes, but is not limited to, club membership dues and assessments, food and beverage expenses, expenses for services furnished by the club, and reimbursements or salary adjustments to officers or employees for any of the preceding expenses.

(2) The term “*club*” means any nonprofit corporation or association of individuals which is the owner, lessee, or occupant of a permanent building or part of a building, membership in which entails the prepayment of regular dues, and which is not operated for a profit other than profits which would accrue to the entire membership including, but not limited to, any chapter, aerie, parlor, lodge, or other local unit of an American national fraternal organization.

A club described in this rule holding an alcoholic beverage license pursuant to Iowa Code chapter 123 must provide on each receipt furnished to a taxpayer a printed statement as follows: “The expenditures covered by this receipt are nondeductible for state income tax purposes.”

53.8(2) *Losses from passive farming activity.* For tax years beginning on or after January 1, 1986, but before January 1, 1987, add the amount of combined losses from passive farming activity in excess of \$25,000.

a. Definitions.

1. The term “*passive activity*” means an activity where the taxpayer’s corporate officers or employees do not materially participate in the activity or provide substantial personal services to the farming business.

2. The terms “*materially participate*” and “*provide substantial services*” mean participating in the decisions involving the operations or management of the farm, actually working the farm with corporate officers or employees, corporate headquarters on the farm, or hiring and discharging employees. A taxpayer may materially participate in a farming activity when the taxpayer’s actual activities are on other than a full-time basis or when the taxpayer does not perform all necessary functions in operating the farm. In this connection, the fact that the taxpayer utilizes contract services to accomplish day-to-day functions of the farm business does not preclude a finding that the taxpayer has materially participated in the farming activity.

When the taxpayer’s activities with respect to a farming operation are not on a full-time basis, or the taxpayer utilizes contract services to accomplish day-to-day functions of the farming business, no single factor is determinative of whether the taxpayer materially participates in the farming operation. However, physical work and participation in management decisions by corporate officers or employees are two principal factors to be considered. In order to be treated as materially participating due to the latter factor, a corporate officer or employee must participate in the financial and management decisions of the farming operation by regularly advising or consulting with other managing parties with respect to management decisions and by regularly overseeing production activities of the farming operation.

Factors which tend to indicate a lack of material participation or providing substantial services include lack of control of the management and operation of the farm, having authority only to discharge the farm manager, having a farm manager who is an independent contractor rather than an employee, and having limited liability for farm losses.

A limited partner (as defined under applicable state law) is treated as not materially participating, or providing substantial personal services, with respect to farming activity. Thus, unless the taxpayer is also a general partner, there is, in effect, a conclusive presumption that the taxpayer has not materially participated in the activity.

3. The term “*farming*” is defined in Section 464(e)(1) of the Internal Revenue Code. This definition is incorporated in this rule for Iowa corporation income tax purposes and is further defined. The term “*farming*” means the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity, including the raising, shearing, feeding, caring for, training, and management of animals. For example, farming includes the raising of fish, poultry, bees, dogs, flowers, or vegetables. Farming does not include the raising or harvesting of trees (other than fruit or nut-bearing trees). For the purposes of this definition, the raising or harvesting of trees includes forestry (i.e., the care and conservation of forests), the timber and logging industries, and the raising of trees for lumber or pulp. Farming includes the raising or harvesting of plants grown for home decoration, aesthetic, or landscaping purposes, including ornamental trees, Christmas trees, house plants that are called trees, and house plants with tree-like qualities (such as scheffleras, Norfolk Island pines, ficus decova, weeping figs, areca palms, and parlor palms).

b. Net losses from passive farming activity deductible under Section 165 of the Internal Revenue Code from businesses, rents, estates, and trusts except losses under Sections 1211 and 1231 of the Internal Revenue Code are combined and netted against income from passive farming activity from businesses, rents, estates, and trusts to determine net income or loss from passive farming activity.

c. A loss from passive farming activity which has been disallowed as a deduction in the current tax year may be carried forward as a deduction allowable to passive farming activity in the first succeeding tax year, provided that the first succeeding tax year begins before January 1, 1987.

53.8(3) *Percentage depletion.* For tax years beginning on or after January 1, 1986, add the amount that percentage depletion of an oil, gas, or geothermal well computed under Section 613 of the Internal Revenue Code is in excess of cost depletion computed under Section 611 of the Internal Revenue Code.

This rule is intended to implement Iowa Code section 422.35 as amended by 1994 Iowa Acts, Senate File 2215.

701—53.9(422) Gains and losses on property acquired before January 1, 1934. Where property was acquired prior to January 1, 1934, the basis as of January 1, 1934, for determining capital or other gains or losses is the higher of cost, adjusted for depreciation allowed or allowable to January 1, 1934, or fair market value as of that date. *City National Bank of Clinton v. Iowa State Tax Commission*, 251 Iowa 603, 102 N.W.2d 381 (1960).

If as a result of this provision a basis is to be used for purposes of Iowa corporation income tax which is different from the basis used for purposes of federal income tax, appropriate adjustment must be made and detailed schedules supplied in the computation of Iowa taxable income.

This rule is intended to implement Iowa Code section 422.35.

701—53.10(422) Work opportunity tax and alcohol fuel credit. Where provided for in the Internal Revenue Code, as detailed below, a deduction shall be allowed for the amount of credit to the extent that the credit increased federal adjusted gross income.

53.10(1) For tax years beginning on or after January 1, 1977, the amount of credit allowable for federal work opportunity tax credit as provided for in Section 51 of the Internal Revenue Code shall be a deduction from Iowa taxable income to the extent the credit increased income.

53.10(2) For tax periods beginning on or after January 1, 1980, the amount of credit allowable for the federal alcohol fuels credit as provided for in Section 40 of the Internal Revenue Code shall be a deduction from Iowa taxable income to the extent the credit increased income.

This rule is intended to implement Iowa Code section 422.35 as amended by 1997 Iowa Acts, Senate File 129.

701—53.11(422) Additional deduction for wages paid or accrued for work done in Iowa by certain individuals. For tax years beginning on or after January 1, 1984, a taxpayer which is considered to be a small business corporation, as defined by subrule 53.11(2), is allowed a deduction for 50 percent of the first 12 months of wages paid or accrued during the tax years for work done in Iowa for employees first hired on or after January 1, 1984.

A handicapped individual domiciled in this state at the time of hiring.

An individual domiciled in this state at the time of hiring who meets any of the following conditions:

1. Has been convicted of a felony in this or any other state or the District of Columbia.
2. Is on parole pursuant to Iowa Code chapter 906.
3. Is on probation pursuant to Iowa Code chapter 907 for an offense other than a simple misdemeanor.
4. Is in a work release program pursuant to Iowa Code chapter 904.

An individual, whether or not domiciled in this state at the time of the hiring, who is on parole or probation and to whom the interstate probation and parole compact under Iowa Code chapter 913 applies.

For tax years beginning on or after January 1, 1989, a taxpayer which is considered to be a small business corporation, as defined by subrule 53.11(2) is allowed a deduction for 65 percent not to exceed \$20,000 of the first 12 months of wages paid or accrued during the tax year for work done in Iowa for employees first hired after January 1, 1989, who meet the above criteria.

53.11(1) The additional deduction shall not be allowed for wages paid to an individual who was hired to replace an individual whose employment was terminated within the 12-month period preceding the date of first employment. However, if the individual being replaced left employment voluntarily without good cause attributable to the employer or if the individual was discharged for misconduct in connection with the individual's employment as determined by the Iowa division of job service of the department of employment services, the additional deduction shall be allowed.

The determination of whether an individual left employment voluntarily without good cause attributable to the employer or if the individual was discharged for misconduct is a factual determination which must be made on a case-by-case basis.

53.11(2) The term "small business corporation" includes the operation of a farm but does not include the practice of a profession. The following conditions apply for the purpose of determining what constitutes a small business corporation.

a. A small business corporation shall not have had more than 20 full-time equivalent positions during each of the 26 consecutive weeks within the 52-week period immediately preceding the date on which the individual for whom an additional deduction for wages is taken was hired. Full-time equivalent position means any of the following:

1. An employment position requiring an average work week of 40 or more hours;
2. An employment position for which compensation is paid on a salaried full-time basis without regard to hours worked; or
3. An aggregation of any number of part-time positions which equal one full-time position. For purposes of this subrule each part-time position shall be categorized with regard to the average number of hours worked each week as a one-quarter, half, three-quarter, or full-time position, as set forth in the following table:

| <u>Average Number of Weekly Hours</u> | <u>Category</u> |
|---------------------------------------|-----------------|
| More than 0 but less than 15 | 1/4 |
| 15 or more but less than 25 | 1/2 |
| 25 or more but less than 35 | 3/4 |
| 35 or more | 1 (full-time) |

b. A small business corporation shall not have more than \$1 million in annual gross revenues or after July 1, 1984, \$3 million in annual gross revenues or as the average of the three preceding tax years. "Annual gross revenues" means total sales, before deducting returns and allowances but after deducting corrections and trade discounts, sales taxes and excise taxes based on sales, as determined in accordance with generally accepted accounting principles.

c. A small business corporation shall not be an affiliate or subsidiary of a business which is dominant in its field of operation. "Dominant in its field of operation" means having more than 20 full-time equivalent employees and more than \$1 million of annual gross revenues or after July 1, 1984, \$3 million of annual gross revenues or as the average of the three preceding tax years. "Affiliate or subsidiary of a business dominant in its field of operations" means a business which is at least 20 percent owned by a business dominant in its field of operation, or by partners, officers, directors, majority stockholders, or their equivalent, of a business dominant in that field of operation.

d. "Operation of a farm" means the cultivation of land for the production of agricultural crops, the raising of poultry, the production of eggs, the production of milk, the production of fruit or other horticultural crops, grazing or the production of livestock. Operation of a farm shall not include the production of timber, forest products, nursery products, or sod and operation of a farm shall not include a contract where a processor or distributor of farm products or supplies provides spraying, harvesting or other farm services.

e. "The practice of a profession" means a vocation requiring specialized knowledge and preparation including but not limited to the following: medicine and surgery, podiatry, osteopathy, osteopathic medicine and surgery, psychology, psychiatry, chiropractic, nursing, dentistry, dental hygiene, optometry, speech pathology, audiology, pharmacy, physical therapy, occupational therapy, mortuary science, law, architecture, engineering and surveying, and accounting.

53.11(3) Definitions.

a. The term “*handicapped person*” means any person who has a physical or mental impairment which substantially limits one or more major life activities, has a record of such impairment, or is regarded as having such an impairment.

The term handicapped does not include any person who is an alcoholic or drug abuser whose current use of alcohol or drugs prevents the person from performing the duties of employment or whose employment, by reason of current use of alcohol or drugs, would constitute a direct threat to the property or the safety of others.

b. The term “*physical or mental impairment*” means any physiological disorder or condition, cosmetic disfigurement, or anatomical loss affecting one or more of the following body systems: neurological; musculoskeletal; special sense organs; respiratory, including speech organs; cardiovascular; reproductive; digestive; genitourinary; hemic and lymphatic; skin and endocrine; or any mental or psychological disorder, such as mental retardation, organic brain syndrome, emotional or mental illness, and specific learning disabilities.

c. The term “*major life activities*” means functions such as caring for one’s self, performing manual tasks, walking, seeing, hearing, speaking, breathing, learning, and working.

d. The term “*has a record of such impairment*” means has a history of, or has been misclassified as having, a mental or physical impairment that substantially limits one or more major life activities.

e. The term “*is regarded as having such an impairment*” means:

1. Has a physical or mental impairment that does not substantially limit major life activities but that is perceived as constituting such a limitation;

2. Has a physical or mental impairment that substantially limits major life activities only as a result of the attitudes of others toward such impairment; or

3. Has none of the impairments defined as physical or mental impairments, but is perceived as having such an impairment.

f. The term “*successfully completing a probationary period*” includes those instances where the employee quits without good cause attributable to the employer during the probationary period or was discharged for misconduct during the probationary period.

g. The term “*probationary period*” means the period of probation for newly hired employees, if the employer has a written probationary policy. If the employer has no written probationary policy for newly hired employees, the probationary period shall be considered to be six months from the date of hire.

53.11(4) If a newly hired employee has been certified as either a vocational rehabilitation referral or an economically disadvantaged ex-convict for purposes of qualification for the targeted jobs tax credit under Section 51 of the Internal Revenue Code, that employee shall be considered to have met the qualifications for the additional wage deduction.

A vocational rehabilitation referral is any individual certified by a state employment agency as having a physical or mental disability which, for the individual, constitutes or results in a substantial handicap to employment. In addition, the individual must have been referred to the employer after completion or while receiving rehabilitation services pursuant to either a state or federal approved vocational rehabilitation program.

For all other newly hired employees, the employer has the burden of proof to show that the employees meet the qualifications for the additional wage deduction.

53.11(5) The taxpayer shall include a schedule with the filing of its tax return showing the name, address, social security number, date of hiring and wages paid of each employee for which the taxpayer claims the additional deduction for wages.

53.11(6) If the employee for which an additional deduction for wages was allowed fails to successfully complete a probationary period and the taxpayer has already filed an Iowa corporation income tax return taking the additional deduction for wages, the taxpayer shall file an amended return adding back the additional deduction for wages. The amended return shall state the name and social security number of the employee who failed to successfully complete a probationary period.

53.11(7) For tax years ending after July 1, 1990, a taxpayer who did not qualify for the additional deduction for wages paid or accrued for work done in Iowa by certain individuals set forth above is allowed an additional deduction of 65 percent not to exceed \$20,000 of the first 12 months of wages paid or accrued for work done in Iowa for employees first hired on or after July 1, 1990, if the new employee is:

a. An individual domiciled in this state at the time of the hiring who meets any of the following conditions:

- (1) Has been convicted of a felony in this or any other state or the District of Columbia.
- (2) Is on parole pursuant to Iowa Code chapter 906.
- (3) Is on probation pursuant to Iowa Code chapter 907, for an offense other than a simple misdemeanor.
- (4) Is in a work release program pursuant to Iowa Code chapter 904, division IX.

b. An individual, whether or not domiciled in this state at the time of the hiring, who is on parole or probation and to whom the interstate probation and parole compact under Iowa Code section 907A.1 applies.

The additional deduction is not allowed for wages paid to an individual who was hired to replace an individual whose employment was terminated within the 12-month period preceding the date of first employment. However, if the individual being replaced left employment voluntarily without good cause attributable to the employer or if the individual was discharged for misconduct in connection with the individual's employment as determined by the Iowa division of job service of the department of employment services, the additional deduction is allowed.

The determination of whether an individual left employment voluntarily without good cause attributable to the employer or if the individual was discharged for misconduct is a factual determination which must be made on a case-by-case basis.

The taxpayer must include a schedule with the filing of its tax return showing the name, address, social security number, date of hiring, and wages paid of each employee for whom the taxpayer claims the additional deduction for wages.

If the employee for whom an additional deduction for wages was allowed fails to successfully complete a probationary period and the taxpayer has already filed an Iowa corporation income tax return taking the additional deduction for wages, the taxpayer must file an amended return adding back the additional deduction for wages. The amended return must state the name and social security number of the employee who failed to successfully complete a probationary period.

This rule is intended to implement Iowa Code sections 16.1 and 422.35.

701—53.12(422) Federal income tax deduction. “Federal income taxes” shall mean those income taxes paid or payable to the United States Government and shall not include taxes paid or payable or taxes deemed to have been paid to a foreign country. *Construction Products, Inc. v. Briggs, State Board of Tax Review*, Case No. 25, February 1, 1972. “Federal income taxes” includes the federal alternative minimum tax. For tax years beginning on or after January 1, 1990, and before January 1, 1996, “federal income taxes” includes the federal environmental tax. Because the federal environmental tax is deducted in computing federal taxable income and Iowa Code subsection 422.35(4) only allows a deduction for 50 percent of the federal income tax paid or accrued, the federal environmental tax deducted in computing federal taxable income must be added to federal taxable income.

53.12(1) Cash basis taxpayer.

a. When a taxpayer is reporting on the cash basis, 50 percent of the amount of federal income taxes actually paid during the taxable period is allowable as a deduction, whether or not such taxes represent the preceding year's tax or additional taxes for prior years. Fifty percent of a federal tax refund shall be reported as income in the year received.

b. A corporation reporting on the cash basis may deduct 50 percent of the federal income tax on the accrual basis if an election is made upon filing the first return. If the corporation claims an accrual deduction on the first return, it shall be considered as an election. Once the election is made, the corporation may change the basis of federal income tax deduction only with the permission of the director. If a change in accounting method is approved or required by the Internal Revenue Service, the director is deemed to have approved the change in the basis of the federal tax deduction.

c. The federal income tax deduction during the transitional period following a change in accounting method from cash to accrual is the accrual deduction in the year of change, plus any cash payment of federal income tax paid in the year of the change for the tax year prior to the change in accounting method, reduced by a refund of federal income tax paid for the tax year prior to the year of the change in accounting method received in the year of the change. For the year of change and years subsequent to the year of the change, the deduction shall be the accrual deduction plus any federal income tax paid for a tax year prior to the year of change as a result of an amended federal return or federal audit, reduced by any refund of federal income tax paid for a tax year prior to the year of the change in accounting method.

d. The federal income tax deduction during the transitional period following a change in accounting method from accrual to cash is the cash deduction in the year of change, plus any cash payment of federal estimated income tax paid in the year prior to the year of the change for the year of the change. Any refund of federal income tax from a tax year prior to the year of the change received in the year of the change or in a subsequent year is properly accrued to the prior tax year. Any payment of federal income tax due to an amended return or federal audit for a tax year prior to the year of the change made in the year of the change or a subsequent year is accrued to that prior tax year. (For information on amended returns, see 701—subrule 52.3(4).)

53.12(2) Accrual basis taxpayer.

a. The amount of federal income tax to be allowed as a deduction for an accrual basis taxpayer is limited to 50 percent of the actual federal income tax liability for that year.

b. Additional federal income taxes and refunds of federal income taxes (except for 53.12(2) "c") shall be a part of the tax liability accrued for such prior years.

c. Refunds resulting from net operating loss carrybacks, investment credit carrybacks, unused excess profits tax credits, and similar items shall be included in income for Iowa corporation income tax purposes in the year in which such refunds are legally accrued.

53.12(3) Rescinded, effective February 2, 1977.**53.12(4) Consolidated federal income tax allocation.**

a. When a corporation joins with at least one other corporation in the filing of a consolidated federal income tax return, the allowable deduction shall be 50 percent of the consolidated federal income tax liability allocable to that corporation. The allocation of the consolidated federal income tax shall be determined as follows: The net consolidated federal income tax liability is multiplied by a fraction, the numerator of which is the taxpayer's federal taxable income as computed on a separate basis, and the denominator of which is the total federal taxable incomes of each corporation included in the consolidated return. If the computation of the taxable income of a member results in an excess of deductions over gross income such member's taxable income shall be zero. *Sibley State Bank v. Bair, State Board of Tax Review*, Docket No. 182, May 26, 1978. *Internorth, Inc., and Northern Propane Gas Company v. Iowa State Board of Tax Review, Iowa Department of Revenue and Gerald D. Bair, Director of Revenue*, 333 N.W.2d 471 (Iowa 1983).

b. If a corporation joins with at least one other corporation in the filing of a consolidated federal income tax return, the federal income tax deduction allowed the Iowa taxpayer shall not exceed 50 percent of the consolidated federal income tax liability.

This rule is intended to implement Iowa Code section 422.35.

701—53.13(422) Iowa income taxes. Iowa corporation income taxes paid or accrued during the tax year as may be applicable under the method of filing are permissible deductions for federal corporation income tax purposes, but are not for purposes of determining Iowa net taxable income. To the extent taxes were deducted in the determination of federal taxable income, they shall be added to federal taxable income for Iowa corporation income tax purposes. Refunds of Iowa income tax to the extent that the refunds were included in the determination of federal taxable income shall be subtracted from federal taxable income.

This rule is intended to implement Iowa Code section 422.35.

701—53.14(422) Method of accounting, accounting period. The return shall be computed on the same basis and for the same accounting period as the taxpayer's return for federal corporation income tax purposes. Permission to change accounting methods or accounting periods for corporation tax purposes is not required provided the taxpayer furnishes the department with a copy of the federal consent.

This rule is intended to implement Iowa Code section 422.35.

701—53.15(422) Consolidated returns.

53.15(1) Definition. The term "common parent" as used in these rules shall have the same general meaning as when used in the federal income tax regulation. However, where the common parent is not subject to the Iowa income tax because of the provisions of 701—subrule 52.1(1) or because of specific exemption under Iowa Code section 422.34, the common parent shall designate as the agent for the affiliated group, one of its subsidiaries subject to the Iowa income tax and shall notify the director of the same in writing. Where the common parent has designated one of its subsidiaries to act as agent for the affiliated group, reference in this rule to "common parent" shall mean the designated agent.

Unless otherwise distinctly expressed, the terms used in this rule shall have the same meaning as when used in a comparable context in the federal income tax regulations for consolidated returns except for determining whether an affiliated group had exercised its privilege of filing a consolidated return. All references to the "commissioner" or "district director" in the federal regulations shall be construed to mean the director for purposes of the Iowa rules.

a. An affiliated group of corporations which did not file a consolidated return for the immediately preceding taxable year may file a consolidated return in lieu of separate returns for the taxable year. Each corporation which is subject to the Iowa corporation income tax or is unitary with a member which is subject to the Iowa corporation income tax and has been a member during any part of the taxable year for which the consolidated return is to be filed must consent (as provided in paragraph 53.15(1) "d") to the filing of the consolidated return. For tax years beginning on or after July 1, 1992, only those members of the affiliated group of corporations which are subject to the Iowa corporation income tax may be included in the Iowa consolidated return. If the statutory change in the members of an affiliated group of corporations which may be included in an Iowa consolidated income tax causes a change in the members of the affiliated group actually included in the Iowa consolidated income tax return for the previous tax year, the taxpayer may discontinue filing a consolidated Iowa corporation income tax return for the first tax year beginning on or after July 1, 1992.

b. If a group wishes to exercise its privilege of filing a consolidated return, the consolidated return must be filed not later than the date prescribed by Iowa Code section 422.21 (including extensions of time) for the filing of the common parent's return. The consolidated return may not be withdrawn after the last day for filing (including extensions of time) but the group may change the basis of its return at any time prior to the last day.

c. The consolidated return shall be made on Form IA-1120 for the group by the common parent corporation. The common parent corporation of the group must attach a copy of the federal Form 851 (Affiliations Schedule) to the consolidated return.

d. If a group wishes to exercise its privilege of filing a consolidated return, each subsidiary must consent to the filing of the consolidated return for the year. The subsidiaries must consent to the filing of an Iowa consolidated return by joining in the filing of an Iowa consolidated return on or before the due date (including any extensions of time). If both separate and consolidated returns are filed on or before the due date (including any extensions of time), the latest returns filed will be considered as the taxpayers' election in regards to the filing of separate or consolidated returns.

e. The common parent, for all purposes other than the making of the consent required by subrule 53.15(1) "a," shall be the sole agent for each subsidiary in the group, duly authorized to act in its own name in all matters relating to the tax liability for the consolidated return year. No subsidiary shall have authority to act for or to represent itself in any matter. The provisions of this paragraph shall apply whether or not a consolidated return is made for any subsequent year and whether or not one or more subsidiaries have become or have ceased to be members of the group at any time. If a subsidiary has ceased to be a member of the group and if the subsidiary files written notice of the cessation with the director, then upon request of the subsidiary, the director will furnish it with a copy of any notice of deficiency in respect of the tax for a consolidated return year for which it was a member. The filing of the written notification and request by a corporation shall not have the effect of limiting the scope of the agency of the common parent.

f. Unless the director agrees to the contrary, an agreement entered into by the common parent extending the time within which a notice of deficiency may be issued, or a levy or a proceeding in court begun in respect of the tax for a consolidated return year shall be applicable to each corporation which was a member of the group during any part of the taxable year and to each corporation, the income of which was included in the consolidated return for the taxable year, notwithstanding that the liability of the corporation is subsequently computed on the basis of a separate return under these rules.

g. If the common parent corporation contemplates dissolution, or is about to be dissolved, or if for any other reason its existence is about to terminate, it shall forthwith notify the director of that fact and designate another member to act as its agent in its place to the same extent and subject to the same conditions and limitations as are applicable to the common parent. If this notice is not given by the common parent, the remaining members may, subject to the approval of the director, designate another member to act as agent, and notice of the designation shall be given to the director. Until a notice in writing designating a new agent has been approved by the director, any notice of deficiency or other communications mailed to the common parent shall be considered as having been properly mailed to the agent of the group. If the director has reasons to believe that the existence of the common parent has terminated, the director may, if deemed advisable, deal directly with any member in respect of its liability.

53.15(2) *When director may require consolidated return.* In accordance with the provisions of rule 53.15(422), the director may require a consolidated return for those members of an affiliated group of corporations which would be eligible to elect to consolidate their incomes under Iowa Code section 422.37 if the filing of separate returns for such corporations would improperly reflect the taxable incomes of said corporations or of said group.

53.15(3) *Discontinuance of filing consolidated returns.*

a. An affiliated group which filed (or was required to file) a consolidated return for the immediately preceding taxable year is required to file a consolidated return for the taxable year unless it is allowed to discontinue filing consolidated returns, or unless a federal consolidated return is not filed by the group.

b. In the event that a consolidated filing for Iowa tax purposes is discontinued for any reason, the common parent shall so notify the department by letter. The mere filing of separate returns does not, in itself, constitute sufficient notice.

c. The following constitute factors for determining when consolidated filing for Iowa tax purposes can be discontinued:

1. If the filing of separate returns will more clearly disclose the taxable income of each member of the affiliated group. Corporations should note that such determination is vested in the director. Therefore, corporations should make application to the director within a reasonable time prior to the due date of the return (including extensions of time). Normally, this would be not later than 90 days prior to said due date. The application should set forth in detail the taxable income on both a consolidated and separate basis together with the reasons why separate returns would more clearly disclose Iowa taxable income. The mere fact that the consolidated tax liability is greater or less than the combined separate liabilities is not, of itself, a ground for discontinuance of consolidated filing.

2. If one or more of the members of the affiliated group cease to be subject to Iowa corporate income tax or cease to have operations which constitute a part of the unitary business of one or more members subject to the Iowa tax, consolidation may be discontinued in whole or in part.

3. If one or more of the members of the affiliated group change in character so that they are no longer taxable under the Iowa corporate income tax law.

EXAMPLE: Common parent A is a manufacturer. Subsidiary B is a company engaged in small loans. A and B file consolidated Iowa returns. In a subsequent taxable year, B changes its business by surrendering its small loan company license and obtains a state bank charter. Even though A and B continue to file federal consolidated returns, B is now a corporation exempt from tax under Iowa Code section 422.34. Therefore A and B should discontinue filing Iowa consolidated returns.

4. If the affiliated group is purchased by another corporation or affiliated group so that after the purchase the stockholders own less than 50 percent of the fair market value of all classes of outstanding stock of the new corporation or affiliated group then the old group must discontinue filing Iowa consolidated returns. The new group may exercise its privilege of filing a consolidated return.

d. If a group is allowed to discontinue filing consolidated returns for any taxable year, then each member of the affiliated group subject to Iowa tax must file a separate return for such year on or before the last day prescribed by law (including extensions of time) for the filing of the consolidated return for such year.

e. A group shall be considered as remaining in existence, for the purposes of the Code, in accordance with the rules prescribed in Treasury Regulation Section 1.1502-75(d).

f. If a consolidated return erroneously includes the income of one or more corporations which were not members of the group at any time during the consolidated return year, the tax liability of such corporations will be determined upon the basis of separate returns (or a consolidated return of another group, if paragraph 53.15(1) “*c*” or 53.15(3) “*a*” applies) and the consolidated return will be considered as including only the income of the corporations which were members of the group during that taxable year.

g. In any case in which amounts have been assessed and paid upon the basis of a consolidated return, and where the tax liability of one or more of the corporations included in the consolidated return is to be computed in the manner described in paragraph 53.15(3) “*f*,” the amounts so paid shall be allocated between the group composed of the corporations properly included in the consolidated return and each of the corporations, whose tax liability is to be computed on a separate basis (or on the basis of a consolidated return of another group) in such manner as the corporations which were included in the consolidated return, and where the tax liability of one or more of the corporations included absence of an agreement, the tax liability of the group shall be allocated under subrule 53.12(4).

h. The taxable year of members of the group, including rules for changing the parent’s taxable year, income to be included in the separate returns, and the time for making separate returns for periods not included in a consolidated return for the purposes of the Iowa Code, shall be in accordance with the rules prescribed in Treasury Regulation Section 1.1502-76(a)-(c).

53.15(4) *Determination of consolidated Iowa income.*

a. Unless otherwise provided by these rules or manifestly inconsistent with the provisions of the Iowa Code, the consolidated taxable income for a consolidated return year under the Iowa Code shall be determined in the same manner and under the same procedures, including intercompany adjustments and eliminations, as are required by the federal income tax regulations in the case of a federal consolidated return.

b. If the Iowa affiliated group differs in its members from the federal affiliated group, such non-qualifying member(s) shall not be considered includable corporations and all computations hereunder shall be made as if such member(s) were not members of the affiliated group. The consolidated federal income tax liability shall be allocated between includable corporations and nonincludable corporations by subrule 53.12(4).

c. The apportionment provisions of Iowa Code section 422.33 shall be taken into account by an affiliated group doing business within and without Iowa. All members of an affiliated group which join in the filing of an Iowa consolidated return shall determine the portion of the consolidated net income earned within and without Iowa by the same method. All intercompany transactions shall be eliminated in the determination of the apportionment factors.

The gross receipts of each corporation which joins in the filing of an Iowa consolidated corporation income tax return shall be included in the computation of the business activity ratio. The gross receipts of each corporation shall be included in the numerator of the business activity ratio to the extent that it has nexus in Iowa and its gross receipts are not eliminated by intercompany adjustments and are considered Iowa gross receipts by rules 701—54.2(422) to 54.8(422). The gross receipts of each corporation shall be included in the denominator of the business activity ratio to the extent its gross receipts are not eliminated by intercompany adjustments.

53.15(5) Schedules. Supporting schedules shall be filed with the consolidated return. The statement of gross income and deductions and other schedules required for each corporation shall be prepared and filed in columnar form so that the details of the items of gross income, deductions, and credits for each member may be readily ascertained. A column shall also be provided giving effect to any eliminations and adjustments. The items included in the column for eliminations and adjustments should be symbolized to identify contra items affected, and suitable explanations appended, if necessary. Similar schedules shall contain in columnar form a reconciliation of retained earnings for each corporation, together with a reconciliation of consolidated retained earnings. Consolidated balance sheets at the beginning and close of the taxable year of the group shall accompany the consolidated return prepared in a form similar to that required for other schedules. Transactions with a subsidiary which is not included as part of the Iowa consolidated return shall not be considered as intercompany transactions for elimination purposes in computing the consolidated Iowa taxable income for the return period.

53.15(6) Liability for tax.

a. Except as provided in paragraph 53.15(6) “b,” the common parent corporation and each subsidiary subject to the Iowa corporation income tax which was a member of the affiliated group during any part of the consolidated return year shall be severally liable for the tax for the year computed in accordance with Iowa Code chapter 422, on or before the due date (not including extensions of time) for the filing of the consolidated return for that year.

b. If a subsidiary has ceased to be a member of the group and if the cessation resulted from a bona fide sale or exchange of its stock for fair value and occurred prior to the date upon which any deficiency is assessed, the director may make an assessment and collection of the deficiency from the former subsidiary in an amount not exceeding the portion of the deficiency which the director may determine to be allocable to it. If the director makes assessment and collection of any part of a deficiency from the former subsidiary, then for purposes of any credit or refund of the amount collected from the former subsidiary the agency of the common parent under the provisions of paragraph 53.15(1) “e” shall not apply.

c. No agreement entered into by one or more members of the affiliated group with any other member of the group shall in any case have the effect of reducing the liability prescribed under this subrule.

53.15(7) Computation of contribution. Computation of a separate corporation’s contribution to consolidated income or net operating loss subject to Iowa tax for purposes of net operating loss carryover and carryback limitations shall be as follows:

$$\frac{A}{B} \times C \times \frac{D}{A} + E = \begin{array}{l} \text{separate corporation contribution to} \\ \text{consolidated income subject to Iowa tax.} \end{array}$$

A = Separate corporation gross sales within and without Iowa after elimination of all intercompany transactions.

B = Consolidated gross sales within and without Iowa after elimination of all intercompany transactions.

C = Iowa consolidated net income subject to apportionment.

D = Separate corporation gross sales within Iowa after elimination of all intercompany transactions.

E = Separate corporation income allocable to Iowa.

53.15(8) Limitations on net operating loss carryover and carryback.**a. Definitions.**

(1) The term “separate return year” means a year in which a corporation filed a separate return and also a year for which it joined (or was required to join) in the filing of an Iowa consolidated return by another affiliated group.

(2) The term “separate return limitation year” means any separate return year of a member of the group or of a predecessor of the member.

b. Limitation on net operating loss carryover. A net operating loss from a separate return limitation year of a member of the group may be carried over only to the extent that the member contributed to the Iowa consolidated taxable income as computed under subrule 53.15(7). A net operating loss carryover from a separate return limitation year cannot create or increase a consolidated net operating loss which is carried back.

A consolidated net operating loss may be carried over to a consolidated return year without limitation even though in the carryover year the affiliated group contains members which were not members of the group in the loss year.

If a member of the affiliated group in the loss year leaves the group through the sale of its stock or because it is now a corporation exempt from tax under Iowa Code section 422.34, its share, as determined by subrule 53.15(7), of the unabsorbed consolidated net operating loss at the end of the consolidated return year during which the member left the group or became exempt from tax may not be carried forward to a subsequent consolidated return.

c. Limitation on net operating loss carryback. A member’s share of an Iowa consolidated net operating loss as computed under subrule 53.15(7) must be carried back to a separate return year, unless the affiliated group elected to carry the net operating loss forward. However, if the member was not in existence in the carryback year but had been a member of the group for every tax year of its existence, its share of the Iowa consolidated loss may be carried back to a separate return year of the common parent.

If a consolidated net operating loss is carried back to a consolidated return year and all members of the affiliated group are the same in the carryback year as in the loss year, the consolidated net operating loss may be carried back without limitation. If there are members of the affiliated group in the loss year which were not members in the carryback year, then the formula in subrule 53.15(7) must be used to determine the portion of the consolidated net operating loss attributable to the members in existence in the carryback year and which may be carried back. Any member of the affiliated group which was a member of the loss-year affiliated group which has been a member of the group since its formation will be regarded as having been a member of the group in the carryback year even though it was not then in existence. A merger or liquidation of members within the affiliated group will be disregarded in determining whether there has been a change in the group between the loss year and the carryback year.

The amount of net operating loss that may be carried back from a separate return year to a consolidated return year is limited to the extent that the former member contributed to the Iowa consolidated taxable income as computed under subrule 53.15(7).

This rule is intended to implement Iowa Code sections 422.35 and 422.37 as amended by 1992 Iowa Acts, Second Extraordinary Session, Senate File 2393.

701—53.16(422) Federal rulings and regulations. In determining whether “taxable income,” “net operating loss deduction” or any other deductions are computed for federal tax purposes under, or have the same meaning as provided by, the Internal Revenue Code, the department will use applicable rulings and regulations that have been duly promulgated by the Commissioner of Internal Revenue, unless the director has created rules and regulations or has exercised discretionary powers as prescribed by statute which call for an alternative method for determining “taxable income,” “net operating loss deduction,” or any other deductions, or unless the department finds that an applicable Internal Revenue ruling or regulation is unauthorized according to the Iowa Code.

This rule is intended to implement Iowa Code section 422.35.

701—53.17(422) Depreciation of speculative shell buildings.

53.17(1) For tax years beginning on or after July 1, 1992, speculative shell buildings constructed or reconstructed after that date may be depreciated as 15-year property under the accelerated cost recovery system of the Internal Revenue Code. If the taxpayer has deducted depreciation on the speculative shell building on the taxpayer’s federal income tax return, that amount of depreciation must be added to the federal taxable income in order to deduct depreciation under this rule.

53.17(2) On sale or other disposition of the speculative shell building, the taxpayer must report on the taxpayer’s Iowa corporation income tax return the same gain or loss reported on the taxpayer’s federal corporation income tax return. If, while owned by the taxpayer, the building is converted from a speculative shell building to another use, the taxpayer must deduct the same amount of depreciation on the taxpayer’s Iowa tax return as is deducted on the taxpayer’s federal tax return.

53.17(3) For the purposes of this rule, the term “speculative shell building” means a building as defined in Iowa Code section 427.1, subsection 41.

This rule is intended to implement Iowa Code section 422.35.

701—53.18(422) Deduction of multipurpose vehicle registration fee. For tax years beginning on or after January 1, 1992, corporations may claim a deduction for 60 percent of the amount of the registration fee paid for a multipurpose vehicle under Iowa Code section 321.124, subsection 3, paragraph “h.” In order to qualify for this deduction, no part of the multipurpose vehicle registration fee may have been deducted as an ordinary and necessary business expense.

This rule is intended to implement Iowa Code section 422.35.

701—53.19(422) Deduction of foreign dividends. For tax years beginning on or after January 1, 1992, corporations may claim a deduction based on percentage of ownership as set forth in Section 243 of the Internal Revenue Code for foreign dividends including Subpart F income as defined in Section 952 of the Internal Revenue Code. See *Kraft General Foods, Inc. v. Iowa Department of Revenue and Finance*, 505 U.S. ____ , 120 L.Ed 59, 112 S.Ct. 2365 (1992).

This rule is intended to implement Iowa Code section 422.35.

701—53.20(422) Employer social security credit for tips. Employers in the food and beverage industry are allowed a credit under Section 45B of the Internal Revenue Code for a portion of the social security taxes paid or incurred after 1993 on employee tips. The credit is equal to the employer's FICA obligation attributable to tips received which exceed tips treated as wages for purposes of satisfying minimum wage standards of the Fair Labor Standards Act. The credit is allowed only for tips received by an employee in the course of employment from customers on the premises of a business for which the tipping of employees serving food or beverages is customary. To the extent that an employer takes the credit for a portion of the social security taxes paid or incurred, the employer's deduction for the social security tax is reduced accordingly. For Iowa income tax purposes, the full deduction for the social security tax paid or incurred is allowed for tax years beginning on or after January 1, 1994. No social security tax credit is allowed on the Iowa corporation income tax return.

This rule is intended to implement Iowa Code section 422.35 as amended by 1995 Iowa Acts, chapter 152.

701—53.21(422) Deduction of gifts, grants, or donations. For tax years ending on or after July 1, 1998, to the extent that any gift, grant, or donation to the endowment fund of the Iowa educational savings plan trust made on or after that date has not been deducted in computing federal taxable income, the amount may be deducted for Iowa income tax purposes.

This rule is intended to implement Iowa Code section 422.35 as amended by 1998 Iowa Acts, House File 2119.

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